2001 Country Reports on Economic Policy and Trade Practices
Released by the Bureau of Economic and Business Affairs
U.S. Department of State, February 2002

CHILE

Key Economic Indicators

(Billions of U.S. dollars unless otherwise indicated)

	1999	2000	2001 1/
Income, Production and Employment:			
Nominal GDP 2/	67.7	71.3	63.6
Real GDP Growth (pct) 2/	-1.1	5.4	3.5
GDP Growth by Sector (pct): 2/			
Fishing	1.7	12.1	2.7
Agriculture	-1.3	5.5	3.8
Mining	16.2	4.4	2.8
Manufacturing	-0.7	5.0	5.0
Construction	-10.0	-0.3	6.2
Services	-1.0	4.5	6.2
Government	1.4	2.1	3.0
Per Capita GDP (US$) 2/	4505	4603	4873
Labor Force (000s) 4/	5,934	5,870	5,863
Unemployment Rate (pct) 2/	9.7	9.2	9.4
Money and Prices (annual percentage growth):			
Money Supply Growth (M2) 2/	9.1	7.2	9.4
Consumer Price Inflation (pct) 2/	2.3	4.5	3.1
Exchange Rate (Peso/US$ - annual average) 2/	509	540	715
Balance of Payments and Trade:			
Total Exports FOB 2/	15.6	18.2	18.0
Exports to United States 3/	3.0	3.5	3.7
Total Imports CIF 2/	14.0	16.7	16.9
Imports from United States 3/	3.1	3.3	3.3
Trade Balance 2/	1.6	1.5	1.1
Balance with United States 3/	- 0.2	0.2	0.4
Total External Debt 2/	34.2	36.8	36.9
Private Debt	28.3	31.3	31.8
Public Debt	5.8	5.6	5.2
Fiscal Balance/GDP (pct) 2/	- 1.5	0.1	+1.0
Debt Service Payments/Exports (pct) 2/	27.7	25.4	30.8
Gold and Foreign Exchange			

Reserves (US$ billions) 2/	14.7	14.7	14.1
Aid from United States (US$ millions)	0.3	0.3	0.3
Aid from All Other Sources	N/A	N/A	N/A

1/ 2001 figures are projections.
2/ 2001 dollar value of GDP has declined because of this year's peso depreciation. The 2001 figure is a recent Santander estimate. Other data is Central Bank of Chile.
3/ U.S. Department of Commerce, International Trade Administration Statistics.
4/ National Institute of Statistics, Chile.

1. General Policy Framework

Chile has maintained market-oriented economic policies for nearly three decades. It was the first country in Latin America to implement fully a market-based economic model, including large-scale privatizations of state enterprises, liberalizing wages and prices, instituting fiscal responsibility, lowering barriers to foreign trade significantly and removing barriers to foreign investment. These policies, along with Chile's commitment to an export-oriented growth strategy, have created a modern, competitive economy that has enjoyed exceptionally high rates of growth over the last 15 years. Chile has also succeeded in improving living standards and reducing poverty during that time.

In the late 1990's, Chile's economy fell victim to global fallout from a series of financial crises in various emerging market countries. Economic growth declined significantly along with foreign investment in Chile and demand for the country's leading exports. In 1999, the Central Bank abandoned the exchange band and adopted a policy of targeting inflation using short-term interest rate policy and limited intervention in currency markets. Inflation has remained below five percent since this policy has been in place, and the country's independent Central Bank is expected to keep the price level stable.

While Chile's economy returned to strong growth (five percent) in 2000, it fell victim in 2001 to the worldwide slump and concerns in financial markets over a possible default in Argentina. Unemployment, meanwhile, has remained persistently high for the last two years, and is currently hovering near ten percent, despite large-scale government jobs programs. World prices for copper, which continues to represent approximately 40 percent of Chile's exports, have declined by 28 percent since late 2000. The value of the peso has also declined by over 25 percent in the same time period, but slack domestic demand has so far prevented businesses from passing price hikes on to consumers. Most government and private sector experts expect GDP growth in the range of three to four percent in both 2001 and 2002. Chile's economy continues to attract foreign investment; FDI during the first six months of the year totaled over three billion dollars, surpassing the figure for all of 2000.

The government of President Ricardo Lagos, which assumed power in March 2000, has maintained Chile's longstanding commitment to a disciplined fiscal policy. Over the long term, the Chilean government aims to maintain what it calls a "structural" surplus, basing its planned expenditures on projections of the price of copper and an underlying capacity for economic growth of approximately five percent. The policy is directed at maintaining a limited capacity for counter-cyclical government spending. Chile's level of public foreign debt remains low (less than one percent of GDP), and the country's sovereign bonds are considered investment grade. Chile maintains reserves of over $14 billion dollars, or the equivalent of 10 months of imports. The country's current account deficit in 2001 is expected to equal roughly 2.2 percent of GDP.

In the past year, the Chilean government has enacted several new pieces of legislation that will have an impact on the country's economic climate. Labor reform measures have increased protections of basic worker's rights while seeking to facilitate the hiring of new entrants into the workforce. A new law on taxes has lowered rates for most individuals and increased them slightly on businesses. Meanwhile, the Chilean government has continued its efforts to negotiate free trade agreements (FTAs) with its leading commercial partners. FTA talks with the United States were nearing conclusion at the end of 2001, and Chilean negotiators hope to wrap up similar negotiations with the European Union in mid-2002. Similar discussions are also underway with South Korea and Singapore.

2. Exchange Rate Policies

The Central Bank moved to a freely floating exchange-rate system from an exchange-rate band in September 1999. This represented a significant change from previous policy, which sought to keep the peso/dollar rate within pre-set parameters. The Central Bank now targets inflation via short-term interest rate policy and limited intervention in currency markets to reduce exchange rate volatility. The Bank's target range for inflation is 2-4 percent. In June 2001, the Central Bank cut the main inter-bank interest rate to 3.5 percent, the lowest level in 15 years. The Bank expected to maintain low rates until an eventual economic recovery increases inflationary pressures. Over the last several years, the Central Bank has gradually reduced restrictions on foreign-exchange outflows other than reporting requirements. A legal parallel market operates with rates almost identical to the inter-bank exchange rate.

During 2001, the peso has lost over 25 percent of its value against the dollar. This decline has resulted from the Argentinean economic crisis and from a decline in international demand for Chilean exports and financial instruments. The Central Bank has intervened in exchange markets several times in recent months in order to defend the peso. By mid-October, the central bank had spent approximately $700 million defending the currency. The President of the Central Bank has indicated that The Central Bank is willing to spend an additional $1.3 billion from now until the end of the year to reduce exchange rate volatility.

3. Structural Policies

Pricing policies: The government rarely sets specific prices. Exceptions are urban public transport and some public utilities and port charges. State enterprises generally purchase at the lowest possible price, regardless of the source of the material. Most U.S. exports enter Chile and compete freely with other imports and Chilean products. Chile's trade agreements with Mexico, Canada, Mercosur and Central America give exporters from those countries significant competitive advantages; virtually all Mexican and Canadian exports enter the Chilean market duty free. Import decisions are typically related to price competitiveness and product availability. Certain agricultural products are an exception to both the Government of Chile's practice of making import decisions based on competitiveness, as well as the Government of Chile's policy of not setting prices.

Tax policies: Forty percent of total tax revenues are generated by an 18 percent Value-Added Tax (VAT), which applies to all sales transactions. There is an eight percent tariff on virtually all imports originating in countries with which Chile does not have a free trade agreement, down from 11 percent in 1998. Tariffs are programmed to drop to seven percent in 2002, and to six percent in 2003. Six percent will then become the new base tariff rate. Computers enter Chile duty-free as a result of the WTO Information Technology Agreement.

In August 2001, the Chilean Congress passed a tax reform bill. The new law cuts personal income tax rates across the board with the top marginal rate being cut from 45 percent to 40 percent for income over about $75,000 per year. Persons earning less than approximately $7,000 per year are exempt from income taxes. In order to compensate for the anticipated $150 million in lost revenue, the new tax law raised the corporate tax rate from 15 percent to 17 percent for retained earnings. There is also a 35 percent tax on distributed profits. There are tax incentives in the tax code to promote Foreign Direct Investment, regional development, specific industries, and capital contribution and donations to educational and cultural institutions. All individuals domiciled or resident in Chile are subject to personal income tax on their worldwide income. Nonresidents are taxed on their Chilean-source income only. Individuals working in Chile for periods not exceeding six months in a year are considered non-residents. A Chilean resident corporation is subject to corporate income tax on its worldwide income. A corporation is considered resident if it is incorporated in Chile. A branch of a foreign corporation is taxed on its own worldwide income. However, income derived from certain regions of Chile located in the extreme north and south is exempt from corporate tax. Many smaller enterprises underreport income, but tax evasion is a minor problem.

Regulatory policies: The most heavily regulated areas of the Chilean economy are utilities, the banking sector, securities markets, and pension funds. Other regulations tend to be focussed in labor, environment, and health standards. While no government regulations explicitly discriminate against U.S. exports to Chile, certain health regulations on processed foods have effectively excluded U.S. products, including breakfast cereals and snack foods. Chile’s sanitary regulations have also limited U.S. meat exports to Chile. Other government programs, like the price-band system for some agricultural commodities described below, discourage U.S. exports. In recent years, the government has introduced rules permitting private investment in the construction and operation of public infrastructure projects such as toll roads, and most major infrastructure projects have been developed in this way. The "privatization" of Chilean state-owned ports, which consists of granting long-term concessions for the operation and management of ports, is proceeding as projected, with the major ports already privatized. Concession projects for 2001 include highways, prisons, and airport improvements.

4. Debt Management Policies

Due to Chile's vigorous economic growth, fiscal responsibility and careful debt management over the last decade, the magnitude of foreign debt no longer constitutes a major structural problem. As of August 2001, Chile's public and private foreign debt was $36.9 billion, or 50 percent of GDP (in 1985, the debt-to-GDP ratio was 125 percent). Public-sector debt has remained low the past five years, fluctuating between $5 and $6 billion and representing 7.3 percent of GDP in 2000.

5. Significant Barriers to U.S. Exports

Chile has a relatively open economy and is a member of the WTO. However, many agricultural commodities are subject to strict phytosanitary requirements and restrictions. The uniform eight percent import tariff rate applies to all goods except for used goods, which are subject to a 16.5 percent tariff. Chile has free-trade agreements that will lead to duty-free trade in most products by the early 2000s with Canada, Mexico, Venezuela, Colombia, Ecuador, Peru, Bolivia, El Salvador, Nicaragua, Honduras, Guatemala, Belize, and Mercosur. Chile is also an active participant in negotiations for the Free Trade Area of the Americas (FTAA), and currently is negotiating a free trade agreement with the United States. Negotiations are supposed to be concluded early in 2002. Tariffs also are lower than eight percent for certain products from member countries of the Latin American Integration Association (ALADI).

The 18 percent VAT is applied to the CIF value of imported products plus the eight percent import duty. Duties may be waived for seven years for capital goods imports purchased as inputs for products to be exported. Duties may be waived on capital goods to be used solely for production of exports (see Section 6 below). There is an additional luxury tax of 85 percent on the CIF value of automobiles in excess of $15,000. This tax discourages sales of larger and more expensive vehicles, including many U.S.-made automobiles. Auto sales on the whole have been declining since the 1998 recession. Sales in 2001 are 23.5 percent below those of 2000 and less than 50 percent of auto sales in 1997. General Motors has the greatest market share with 19.8 percent of the market.

Another tax that has had the effect of discouraging U.S. exports was a prejudicial excise tax on distilled liquors that compete with domestically produced liquors. In late 1997 the legislature passed a law to modify gradually, but not eliminate, the discriminatory taxation faced by imported liquors. The European Union won a WTO panel appeal over Chile's discriminatory liquor taxation. The United States was a third party observer to the panels. New WTO compliant laws regarding the taxation of distilled spirits have been passed by the Chilean congress. The United States was a third party observer to the panels.

Import licenses: Import licenses are granted as a routine procedure for most products**.** Imports of used automobiles and most used car parts are prohibited.

Investment barriers: Chile's foreign investment statute, Decree Law (DL) 600, sets the standard of treatment of foreign investors to be the same as that of Chilean investors. DL 600 investment is generally direct investment. Foreign investors using DL 600 sign a contract with the government's Foreign Investment Committee guaranteeing the terms and tax treatment of their investments. These terms include the rights to repatriate profits immediately and capital after one year, to exchange currency at the official inter-bank exchange rate, and to choose between either national tax treatment at 35 percent or a guaranteed rate for the first ten years of an investment at 42 percent. Approval by the Foreign Investment Committee is generally routine, but the committee has rejected some "speculative" investments. In late 1997, the government modified its DL 600 policy to restrict investment entering under the law's provisions to projects worth more than $1 million. In addition, projects of more than $15 million are now routinely vetted with the Central Bank to identify possible "speculative" flows. DL 600 limits foreign loan leveraging to a 1:1 ratio. Associated external loan financing in excess of the value of a direct foreign investment cannot enter under the provisions of DL 600 (i.e., free of deposit requirements).

Outside DL 600 Foreign Investment can enter Chile under Chapter 14 of the Central Bank Regulations. Few firms have used this means of investment, as it lacks the guarantees provided by the contract with the Foreign Investment Committee. The Central Bank has the authority to require that investors deposit a percentage of the value of short-term capital inflows in a non-interest-bearing Central Bank account for as long as two years. This deposit (known as *encaje)* was required by the Bank through mid-1998 and was set at that time at 30 percent for one year. Since 1998, the Bank has not required such deposits and has set the requirement at zero percent. The Bank does, however, retain the right to reinstate the *encaje* in the future.

There is not a tax treaty between Chile and the United States, although negotiations are underway, so profits of U.S. companies operating in Chile are liable to taxation by both governments. However, U.S. firms generally can claim credits on their U.S. taxes for taxes paid in Chile.

There are some deviations, both positive and negative, from the nondiscrimination standard. On the positive side foreign investors receive better than national treatment on taxation, as they have the option of fixing the tax rate they will pay at 42 percent for ten years or paying the prevailing domestic rate, which is at present lower. Examples of less than national treatment include the following:

- D.L. 600 allows the Central Bank to restrict the access of foreign investors to domestic borrowing in an emergency in order to prevent distortion of local financial markets. The Central Bank has never exercised this power.

- Certain sectoral restrictions on foreign investment. With few exceptions, fishing in the country's 200-mile Exclusive Economic Zone is reserved for Chilean-flag vessels with majority Chilean ownership. Such vessels also are the only ones allowed to transport by river or sea between two points in Chile ("cabotage") cargo shipments of less than 900 tons or passengers. The automobile and light truck industry is the subject of trade-related investment measures.

- Oil and gas deposits are reserved for the state. Private investors are allowed concessions, however, and foreign and domestic nationals are accorded equal treatment.

- Services barriers: Full foreign ownership of radio and television stations is allowed, but the principal officers of the firm must be Chilean.

Principal non-tariff barriers: The main trade remedies used by the Chilean government are surcharges, minimum customs values, countervailing duties, antidumping duties, and import price bands and safeguards. A significant non-tariff barrier is the import price-band system for wheat, wheat flour, and sugar. When import prices are below a set threshold, surtaxes are levied on top of the across-the-board eight percent tariff to bring import prices up to an average of international prices over previous years. Domestic flour millers and beverage manufacturers continue to complain bitterly about the high duties on wheat and sugar.   Imports of U.S. wheat are expected to be down in 2001.

Sanitary and phytosanitary requirements: Chile has improved its recognition of pest-free areas in the United States, but delays on approval for many U.S. fruits and vegetables continue to hamper increased sales to Chile. On a positive note, Chile is in the process of granting market access for Oregon and Idaho apples and pears, and California and Arizona citrus.   Chile has begun to publish its regulations and, in some cases, allows a public comment period on proposed rules. Most import permits for processed foods are issued on a case-by-case basis, thereby lending to uncertainty and possible discriminatory treatment. Procedures and tolerances for testing imported chicken for the presence of salmonella present such a severe commercial risk that local importers are reluctant to import such products. Chile's unique beef grading and labeling requirements effectively preclude imports of U.S. beef. Chile’s livestock products law requires first-hand Chilean inspection of every U.S. establishment wishing to export to Chile. Products affected include red meat, dairy and pet food. Chile does not recognize the U.S. livestock products inspection system. Chile is, however, in the process of recognizing the U.S. salmon egg inspection system.

Government procurement practices: The government buys locally produced goods only when the conditions of sale (price, delivery times, etc.) are equal to or better than those for equivalent imports. In practice, given that many categories of products are not manufactured in Chile, purchasing decisions by most state-entities companies are made among competing imports. Requests for public and private bids are published on the Internet.

6. Export Subsidies Policies

Chile offers a few non-market incentives to exporters. For example, paperwork requirements are simplified for nontraditional exporters. The government also provides exporters with quicker returns of VAT paid on inputs than other producers receive.

The most widely used indirect subsidy for exports is the simplified duty drawback system for nontraditional exports. This system refunds to exporters of certain products a percentage of the value of their exports, rather than refunding the actual duty paid on imported inputs to production (as is the case in Chile's standard drawback program). All Chilean exporters may also defer tariff payments on capital imports for a period of seven years. If the capital goods are used to produce exported products, deferred duties can be reduced by the ratio of export sales to total sales. If all production is exported, the exporter pays no tariff on capital imports.

In 1998, the Chilean Congress replaced earlier forestry-sector subsidy legislation with a new law that will be directed mainly toward assisting small farmers. Planting costs will be subsidized by as much as 90 percent for the first 15 hectares and 75 percent for the remainder in the case of small farmers. A maximum of $15 million yearly will be destined for this purpose. Special land-tax exemptions will also be part of the program. Under the previous law, the combined subsidy costs incurred during 1997 totaled $7.7 million, down from $15.3 million in 1996.

7. Protection of U.S. Intellectual Property

Chile's intellectual property regime is basically strong. However, deficiencies in the intellectual property regime have kept Chile on the USTR Special 301 watch list since 1989. Chile belongs to the World Intellectual Property Organization. Legislation intended to bring Chile into compliance with its WTO TRIPS commitments is pending in the Chilean Congress.

Copyrights: Piracy of video and audio tapes has been subject to criminal penalties since 1985. Chilean authorities have taken enforcement measures against video, video game, audio, and computer software pirates in recent years, and piracy has declined in each of these areas. In the mid-1980s the software piracy rate was believed to be around 90 percent; it is currently estimated at roughly 50 percent, believed to be the lowest rate in Latin America. The decline is in part the result of a campaign by the United States and international industry, with the cooperation of Chile's courts and government, to suppress the use of pirated software. Industry sources say that penalties remain low relative to the potential earnings from piracy and that stiffer penalties would help to deter potential pirates. Copyright protection is generally the life of the author plus 50 years.

Trademarks: Chilean law provides for the protection of registered trademarks and prioritizes trademark rights according to filing date. Local use of a trademark is not required for registration. As with the licensing of other intellectual property privileges, contracting parties may freely set payment rates for use of trademarks

Patents: Patents are valid for a nonrenewable term of 15 years. Under Articles 37 and 38 of Law 9,039, the direct uses of natural resources or energy, regardless of whether such uses are newly discovered may not be patented. Chile's patent office processes pharmaceutical patents extremely slowly, and many patent holders have seen their rights degraded by the issuance of marketing approval to unauthorized copies. Protection for confidential data provided to patent and health authorities is inadequate.

Industrial Designs: Industrial designs may be registered for a non-renewable term of 10 years. Packaging may be included in the goods protected as industrial designs if the requirements for new development and originality are met. Industrial designs may not protect clothing designs. Registration for an industrial design is valid for a nonrenewable term of 10 years.

Utility Models: Utility models protect inventions of a lesser inventive degree than patents. Registration of a utility model is valid for a nonrenewable term of 10 years.

Internet Domain Name Registry: Registration of domain names using ".cl" requires a local presence in Chile. Foreign applicants must provide the name and taxpayer number of an administrative contact with a Chilean address. Applications to register domain names containing ".cl" are subject to an initial fee of about $50, which is valid for the first two years of the domain's operation. A maintenance fee of approximately $20 must be paid every two years thereafter.

8. Worker Rights

a. The Right of Association: Most workers have a right to join unions or to form unions without prior authorization, and around 10 percent of the work force belongs to unions. Government employee associations benefited from legislation in 1995 that gave them many of the same rights as unions, although they may not legally strike. On September 11, 2001, the Chilean Congress passed a broad reform of the nation's labor code. Several amendments to the code were designed to strengthen worker protections, especially regarding the ability to organize unions. The new code also sets forth enhanced penalties for anti-union activities.

b. The Right to Organize and Bargain Collectively: During the last decade, the climate for collective bargaining has improved, though unions still face difficulties. Sector-wide collective bargaining is allowed but not mandatory. The process for negotiating a formal labor contract is heavily regulated, a vestige of the statist labor policies of the 1960s. The law also permits worker-management discussions to reach collective agreements without direct union involvement. These agreements are still subject to some government regulations, and have the same force as a collective bargaining agreement.

c. Prohibition of Forced or Compulsory Labor: Forced or compulsory labor is prohibited in the constitution and the labor code and is not practiced.

d. Minimum Age for Employment of Children: Child labor is regulated by law. Children 15 to 18 may be legally employed with permission of parents or guardians and in restricted types of labor. Some children under 15 are employed in the informal economy, which is more difficult to regulate. The Chilean government estimates that roughly 50,000 children between the ages of 6 and 14 work. The majority of these were males from single-parent households headed by women.

e. Acceptable Conditions of Work: Minimum wages, hours of work, and occupational safety and health standards are regulated by law. The legal workweek is 48 hours, although this will be reduced to 45 hours in January 2005. The minimum wage, currently around $150 per month, is set by government, management, and union representatives or by the government if the three groups cannot reach agreement. Lower-paid workers also receive a family subsidy. After rising steadily over the proceeding ten years, minimum wage and wages as a whole have essentially been flat over the past two years. Poverty rates have declined steadily from 46 percent of the population in 1987 to 20.6 percent in 2001.

f. Rights in Sectors with U.S. Investment: Labor rights in sectors with U.S. investment are the same as those specified above. U.S. companies are involved in virtually every sector of the Chilean economy and are subject to the same laws that apply to their counterparts from Chile and other countries. There are no special districts where different labor laws apply.

Extent of U.S. Investment in Selected Industries -- U.S. Direct Investment Position Abroad on an Historical Cost Basis **--** 2000

(Millions of U.S. Dollars)

Category		Amount
Petroleum		73
Total Manufacturing		1,363
Food & Kindred Products	151	
Chemicals & Allied Products	230	
Primary & Fabricated Metals	(D)	
Industrial Machinery and Equipment	17	
Electric & Electronic Equipment	(D)	
Transportation Equipment	(D)	
Other Manufacturing	186	
Wholesale Trade		374
Banking		700
Finance/Insurance/Real Estate		3,557
Services		210
Other Industries		4,569
TOTAL ALL INDUSTRIES		10,846

(D) Suppressed to avoid disclosing data of individual companies.

Source: U.S. Department of Commerce, Bureau of Economic Analysis.